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RECENT DEVELOPMENTS UNDER THE MEXICAN FOREIGN INVESTMENT LAW AND THE LAW REGULATING THE TRANSFER OF TECHNOLOGY*

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and
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INTRODUCTION

This paper summarizes developments since October, 1974 with regard to the administration of the 1973 Mexican laws regulating foreign investment and technology transfer. The paper is divided in four parts, as follows:

1. Part One is an up-date on the statistics of the number of cases processed by the Commission of Foreign Investment and the National Registry for the Transfer of Technology. This part of the paper will group the decisions according to subject matter and will afford a view of the problems of principal concern to both agencies.

*This contribution was received through the courtesy of the Council of the Americas. It is a Joint Paper presented at the XXX Plenary Meeting of the Mexico-U.S. Businessmen's Committee held at Pebble Beach, California, November 12-14, 1975. The Committee, sponsored in Mexico by the Mexican Business Council for International Affairs, and in the United States by the Chamber of Commerce of the United States, the American Chamber of Commerce of Mexico and the Council of the Americas, meets once a year and reviews the relationships between the two countries.

The Joint Paper is considered particularly relevant. The United States businessman's experience with Mexico's foreign investment and transfer of technology laws, constitutes one of those rare instances in which interested parties—in government and private industry—can observe the law in action, as well as a sincere attempt by those intimately concerned to seek accommodation, not confrontation. It is an encouraging sign in government-business relations, and the *Lawyer* is grateful to the Committee, and particularly to the authors of the Joint Paper, for sharing it with its readers.

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2. Part Two of the paper will focus on some of the important situations and issues that have occupied the attention of all concerned with these two laws during the past year. Some of these situations and issues were present last year. Others appeared this year or are on the horizon. Those chosen for discussion crystallize policies and directions of both the Commission and the Registry during the past year. They also provide a basis for questions and constructive suggestions from the businessman's point of view.
3. Part Three contains a report on the progress of the Consultative Task Force Programs. Over the past year and a half the Task Force visits have brought businessmen together with government officials in informal, small meetings, to try to talk out some of the practical operating problems presented by these laws. This program has won the continuing support of the Mexican government.
4. Part Four offers suggestions on how the Mexico-U.S. Businessmen's Committee and its individual members may increase the usefulness of the dialogue with Mexican government officials, represented by the Task Force approach.

PART ONE

Before presenting the pertinent statistical information it is well to note two important developments. First, the appointment of Lic. Jaime Alvarez Soberanis as Director General of the Registry for the Transfer of Technology, following the resignation of Ing. Enrique Aguilar who joined UNIDO in Vienna. Lic. Alvarez was one of two Subdirectors under Ing. Aguilar, and he was in turn substituted by Lic. José Ignacio Campillo. Lic. Alvarez and his staff continue the tradition of dedication, high professionalism and fairness first established at the Registry by Ing. Aguilar. Second, to extend our compliments to Lic. Mauricio de Maria y Campos, Executive Secretary of the Foreign Investment Commission, and his staff for their high professionalism and fairness. Also to note a difference in the structure of the two agencies above which it is believed has an impact on their productivity. The Head of the Registry has more decision-making authority than does the Executive Secretary of the Commission, a difference deliberately written into the laws. While the activity of the Registry is of vital importance to the development goals of Mexico, its decisions are more easily restricted to technical considerations than

those of the Commission. The criteria for approving or denying a proposed foreign investment include broader economic, social and political questions. As a result, although the Executive Secretary of the Commission does have a good deal of influence it was thought advisable to diffuse ultimate decision-making responsibility, for other than routine matters, among the several Ministries that form the Commission: Interior, Foreign Relations, Treasury, Industry and Commerce, Labor, Presidency and National Patrimony.

Foreign Investment

Direct foreign investment, which averaged \$200 million dollars per year for the period 1970-1972, increased to \$287 million in 1973 and to \$362 million in 1974. Preliminary figures for the first six months of 1975 place direct foreign investment at \$215 million, a trend that if continued could result in figures for the year of more than \$400 million. As can be deduced, direct foreign investment is reacting strongly after slowing down in the 1970-1972 period, probably as a result of the enactment of the Foreign Investment Law.

At the end of March 1975 the Commission had issued 10,500 Certificates of Registration, compared with only 900 at the end of August 1974. However, around 80% of those were requests to authorize the appointment of a foreigner to Boards of Directors, or the purchase of small amounts of stock, requests which do not even reach the full Commission and are solved by its Executive Secretary. Since it was formed in May of 1973 and until October 1975, the Commission has passed 249 specific resolutions, compared with 93 at the end of September 1974 and 106 at the end of March 1975. These 249 resolutions are related to the acquisition of an established company by foreigners; investment in new establishments, new lines of products and new fields of economic activity by companies majority-owned by foreigners; acquisition of fixed assets by foreign investors; and the constitution of new companies with foreign participation. Out of 249 resolutions, 201 or 80% have been favorable, compared with only 65 or 68% of the total answered at the end of September 1974.

The 201 positive resolutions represent foreign investment propositions that either from the beginning or after negotiations with the Commission, met the majority of the following criteria:

- * Mexican control of ownership and administration

* Compatibility with national development goals, such as:

- generation of employment
- import substitution and/or exports
- technological development
- industrial decentralization
- diversification of external sources of financing

The 48 or 20% of the negative resolutions issued through October 1975 have been based on the Commission's belief that the proposed investments would have resulted in the displacement of nationals or would not have contributed to our economic priorities and development goals. For example, the field of activity of the proposed investment is of concern, i.e., the possibilities of a positive answer are greater for a project to make capital goods or something not made in Mexico, than for a project in, say, the pharmaceutical or food industries, where the government feels there is too much foreign participation already.

The breakdown of the 249 requests, classified as to their nature, is presented below:

| <u>Nature of request</u> | <u>Number</u> | <u>% of Total</u> |
|--|---------------|-------------------|
| 1. Acquisition of shares: | 163 | 65.5 |
| a. By foreigners from foreigners | 83) | 33.3) |
| b. By foreigners from Mexicans | 34) | 13.6) |
| c. Through mergers | 17) | 6.8) |
| d. Via capital increase | 29) | 11.7) |
| 2. New establishment: | 33 | 13.2 |
| 3. New line of products: | 16 | 6.4 |
| 4. Incorporation of new companies: | 16 | 6.4 |
| 5. Acquisition of more than 49% of assets: | 8 | 3.2 |
| 6. Other: | 13 | 5.2 |
| | <u>249</u> | <u>100.0</u> |

A further breakdown showing both the nature of the project and the kind of reply follows:

| <u>Nature of request</u> | <u>Approved</u> | <u>Denied</u> | <u>Total</u> |
|--|-----------------|---------------|--------------|
| 1. Acquisition of shares: | | | |
| a. By foreigners from foreigners | 81 | 2 | 83 |
| b. By foreigners from Mexicans | 27 | 7 | 34 |
| c. Through mergers | 15 | 2 | 17 |
| d. Via capital increase | 22 | 7 | 29 |
| 2. New establishment: | 20 | 13 | 33 |
| 3. New line of products: | 10 | 6 | 16 |
| 4. Incorporation of new companies: | 8 | 8 | 16 |
| 5. Acquisition of more than 49% of assets: | 8 | — | 8 |
| 6. Other: | 10 | 3 | 13 |
| | <u>201</u> | <u>48</u> | <u>249</u> |

It is evident that the main unresolved issues are associated with the definition of new establishment and new line of products, which will be discussed in greater detail in Part Two. On the other hand, the incorporation of a new company clearly depends for authorization on its alignment with national economic development goals.

Finally, a summary of the ten general resolutions of the Foreign Investment Commission published in the *Diario Oficial* (Official Gazette) last November 5, is presented below:

Number 1 — Authorizes *maquiladoras* to operate with up to 100% foreign ownership, except for those active in the textile industry. The exchange of stock of companies established as *maquiladoras* between foreigners does not require approval from the Commission. All such companies do not need Commission authorization to open new establishments.

Number 2 — Authorizes capital increases of existing companies as long as the relation of Mexican versus foreign ownership that existed when the Law was enacted remains the same. Foreign investors buying shares in a capital increase situation must independently maintain the same relation between the nominal value of their investment and the capital stock of the company that existed when the law was enacted.

Number 3 — Authorizes foreigners to acquire shares for up to 5% of the capital stock in any company through the Stock Exchange.

Number 4 — Authorizes re-election of foreign members of a board of directors.

Number 5 — Authorizes the appointment of foreigners to a board of directors, assuming that the composition of the board is in accordance with the law.

Number 6 — Authorizes the Executive Secretary of the Commission to allow purchases of up to 1% of the capital in any company between foreigners, assuming that at least 96% of the shares are already owned by a foreign investor.

Number 7 — Foreigners with a migratory status of *inmigrado* are considered Mexicans for purposes of company administration and/or company management.

Number 8 — For the purposes of the law, a new establishment is defined as any technical unit or any locale physically independent or different from the existing ones, where a company proposes to undertake any type of activity. For the above mentioned purposes, a new establishment is defined even as the relocation by a company of any of its existing facilities. The above notwithstanding, foreign investors are authorized to open new administrative offices or warehouses as long as no other activity is undertaken in these locations. The establishment or relocation of an establishment which contributes to industrial decentralization will be taken into consideration as a very important element from the point of view of the Commission's resolution.

Number 9 — All trusts established in which foreigners have some specific rights must request registration at the National Registry of Foreign Investments.

Number 10 — Simplifies the procedure to be followed by individual foreign investors who acquire shares on the Stock Exchange.

Transfer of Technology

With respect to the activities of the Registry, a summary of the statistical information available is presented below:

| | <u>To 10/31/74</u> | <u>To 8/31/75</u> |
|---|--------------------|-------------------|
| I. Total number of contracts known to the Registry | | |
| 1. Submitted to take note and pending request for registration: | 3,848 | 1,906 |
| 2. Submitted to take note and cancelled: | 81 | 81 |
| 3. Contracts whose registration has been requested: | 1,977 | 4,595 |
| 4. Total number of contracts known to the Registry: | 5,906 | 6,582 |
| II. Status of contracts submitted to take note only | | |
| 1. Total number of contracts submitted to take note: | 4,112 | 4,112 |
| 2. Contracts submitted to take note and cancelled before 1/29/75: | 81 | 81 |
| 3. Contracts submitted to take note and whose registration was requested later: | n.a. | 2,125 |
| 4. Contracts submitted to take note and which have not been cancelled nor formally submitted for registration to 8/31/75: | n.a. | 1,906 |

| | <u>To 10/31/74</u> | <u>To 8/31/75</u> |
|--|--------------------|-------------------|
| III. Status of contracts formally submitted for registration | | |
| 1. Total number of cases evaluated by Registry: | 1,724 | 3,972 |
| 2. Contracts considered as nonexistent: | 156 | 219 |
| 3. Contracts that have been cancelled: | 60 | 61 |
| 4. Contracts considered as not needing submission: | — | 2 |
| 5. Contracts pending resolution: | 216 | 623 |
| 6. Contracts resolved either way by Registry: | 1,508 | 3,692 |
| a. accepted: | 1,250 | 2,473 |
| b. rejected: | 258 | 1,219 |

It is obvious that the activity of the Registry from February 1, 1973 to October 31, 1974, was characterized by a cautious approach by both the Registry and the parties involved in the transfer of technology, as proven by the high number of contracts submitted to take note only, and the relatively small number of contracts evaluated and resolved during this period. As the Registry acquired a better knowledge of the problems associated with the transfer of technology and accumulated experience, it was able to deal more efficiently with the situation. On the other hand, the parties involved in the process learned more about the administration and motivations of the Registry, thus improving their ability for success in dealing with the staff of the Registry. The difference in the number of contracts evaluated and resolved between October 31, 1974 and August 31, 1975, is evidence of the hard working nature of the Registry's staff and the knowledge and experience they now have of the problem. A comparison of the reasons behind the negative decision of the Registry gives a better view of the problems which are of principal concern to its staff. Accordingly, Art. 7 sections are grouped below by their frequency of citation, for different dates:

| Group | Art. 7 Section | Subject Matter | Percentage | | |
|-------|-------------------|---------------------------------------|------------|----------|---------|
| | | | 3/31/74 | 11/30/74 | 3/31/75 |
| 1 | II | Price and unjustified burdens | 81.3 | 79.7 | 78 |
| 2 | XIII | Unreasonable term | 40.1 | 39.6 | 38 |
| | XI | Output and price restrictions | 39.8 | 38.2 | 35 |
| 3 | V | Limitations on R & D | 26.4 | 23.9 | |
| | VII | Export restrictions | 26.4 | 26.6 | 34 |
| | IV | Grant back requirements | 24.7 | 25.8 | |
| | XIV | Foreign courts and law | 22.7 | 22.2 | |
| 4 | VI | Exclusive purchase requirements | 15.0 | 14.0 | |
| | III | Management intervention | 9.0 | 9.7 | |
| | VIII | Complementary technology prohibitions | 5.0 | 4.8 | |
| 5 | XII | Exclusive sales agent requirements | 2.0 | 1.4 | |
| | I | Existing Mexican technology | 1.3 | 1.2 | |
| | IX | Exclusive sales arrangements | 1.0 | 1.2 | |
| | X | Foreign personnel requirements | 0.3 | 0.2 | |

This comparative analysis permits the conclusion that with a few exceptions, the comments presented by Mr. Hope Camp in October 1974 are still valid. The only two situations that deserve some comment are:

1. A decrease in the importance of Section XI of Art. 7 as an issue, probably more as a consequence of better handling by the parties negotiating a contract than by a significant modification in the position of the Registry.
2. More significant to those buying or selling technology in Mexico is the increasing importance of Section VII as an issue, which results from the ever growing need to export.

PART TWO

This part will focus on some of the more important situations and issues that have arisen under the laws under consideration during the past year. The emphasis will be upon the status of issues that remain unresolved and upon new situations or issues on the horizon. Although there is considerable overlap of issues between the two laws, for clarity of presentation the Foreign Investment Law will be discussed first.

Foreign Investment Law

It is fair to say that this year there is among lawyers and businessmen a much firmer sense of what the law is about than last year. For example, last year a lot of people were unsure whether Art. 5 required that Mexican ownership be represented at the operating management levels of a company, as well as at the Board of Directors level. Absent evidence of an attempt to circumvent the law, it is generally agreed that the requirement of representation of Mexican ownership in the management provided for in Art. 5 only refers to the Board of Directors level.

This sense of better understanding of the scope of the law extends even to the three issues that generated the greatest amount of discussion and disagreement. Those issues are: 1) new line of products; 2) new fields of economic activity; and 3) new establishments.

Before passing to a discussion of these issues it should be noted that they almost invariably involve the activities of a foreign investor who was in business before the effective date of the law. New investments, in the sense of new foreign capital being injected into Mexican economy, are pretty much a routine matter with the foreign investor almost always taking a minority position. There are some exceptions to this rule. The Foreign Investment Commission has permitted isolated new 100% foreign-owned investments where the investment brings special advantages to the country.

Among the factors considered by the Commission in approving such an investment are: employment; regional development in zones 2 and 3; favorable impact on the balance of payments through exports or import substitutes; and, no adverse impact on established national investors or when the investment is not in an area of activity already well covered.

The three issues that have produced the greatest amount of discussion with respect to the Foreign Investment Law are considered next. The question of what is a new establishment is much clearer this year than last year. It clearly includes any new economic unit of a company in which the foreign investment exceeds 49% of the total investment. The concept of economic unit as applied by the Commission embraces warehouses and other support facilities of an operation. The only real area of doubt left with respect to this issue is when a relocated or enlarged unit may be considered a new economic unit. The Commission treats relocations and enlargements differently. It seems that all relocations must be notified to the Commission. Whether they will be approved depends

upon the nature and degree of their economic impact, i.e., advantages or disadvantages to the nation. At approximately this same time last year the Commission would not apply the economic impact criteria unless the relocation increased capacity in a range of between 25% and 30%. At that time the Commission was split on whether to apply the increase of capacity consideration as a threshold issue. There are indications that the Commission may have abandoned that consideration. It is hard to know and we await the publication of the criteria on new establishments which the Commission has promised. If the 25% to 30% capacity increase consideration has been abandoned, any relocation could entail some form of divestment for the foreign investor, unless the relocation produced a favorable economic impact as judged by the Commission.

The Commission may also apply the economic impact criteria to enlargements of existing economic units. It does not appear that the Commission is as stringent in requiring divestment in the case of an enlargement as it is in the case of a relocation. Indeed, it has been reported that expansions of existing locations that required new capital have been permitted.

A word of caution is indicated. An enlargement can have a greater economic impact than a relocation. The nature and magnitude of the enlargement will be measured. In such a case it is believed that the Commission may examine the situation with a view to requiring some form of divestment by the foreign investor.

The questions of what is a new product line and a new field of economic activity were written in the law to cover separate categories. But they tend to overlap in practice and it is hard, therefore, to talk about one without considering the other at the same time. A good example of this overlap comes from the pharmaceutical industry. It is likely that the Commission will not declare the creation of a new product where there has been a shift of manufacturing a product from human use to animal use with little or no change in manufacturing process or raw materials used. On the other hand, the Commission is uncertain whether such a shift constitutes entry into a new field of economic activity. The marketing of a product for animal use may be different than the marketing of a product for human use. The Commission has indicated that such a change in marketing practice should be registered.

Some general definitions for both categories have emerged in the discussions of the past year. With respect to new product lines it appears

that a new *model* of a product with the same end-use will not encounter objections. For example, new drugs in the same category have been introduced in Mexico this past year without being registered under the law. Further, if the final product is the same, even though different raw materials are used, the Commission will not condition production on some form of divestment. The Commission cautions, however, that any new or different raw materials used in the manufacture of the product must not come from sectors restricted to foreigners in such a manner as to permit foreign control of those sectors.

In general, the Commission will find entry into a new field of economic activity where there has been a shift in manufacturing from one end-use to another. The same findings will be made where there has been a shift in manufacturing for end-use to manufacturing raw materials or intermediate products. Also a shift from a manufacturing activity to a marketing activity constitutes entry into a new field of economic activity. As noted earlier, in the example of a shift in marketing a product from human use to animal use, the Commission is uncertain whether this constitutes entry into a new field of economic activity.

New issues are considered next. Some of these were considered by the Commission in actual cases during the past year. Others are prominently featured in the PRI Basic Government Plan for 1976-1982.

The first issue involves the acquisition of the investment of one foreigner by another foreigner in a business that existed before the effective date of the law. The law provides that approval is required when the acquisition involves more than 25% of the capital or more than 40% of the fixed assets of the business. The Commission applied this provision in a case where the heir of a deceased foreign investor inherited the investment. While the law would seem to cover such a situation, concern has been expressed that the Commission would take an active decision on whether to permit the transfer. It was thought that such a transfer would be automatic.

Several instances have arisen where a merger was agreed upon by two parties with businesses outside the Republic of Mexico. The holdings of the seller included a subsidiary in the Republic of Mexico which was foreign controlled. The Commission actively considered whether to permit the foreign buyer to acquire the foreign interest in the Mexican subsidiary. In two of these cases approval was granted for the foreign acquisition without requiring a prior divestment. We understand that one case is still pending.

These kinds of special situations may seem obvious in retrospect, but they were not foreseen by the parties involved. Thus, they may serve as another reminder that the broad language of the law requires *all* businessmen and their lawyers to consider consequences of a foreign investment in Mexico, apart from the obvious threshold requirement such as minority foreign ownership and voting control in the hands of nationals.

Next is the issue of economic control which is to be contrasted with the control of the business that derives directly from ownership and voting control. This issue has been suggested in the PRI Basic Government Plan for 1976-1982. This plan expresses the basic policy of the ruling party which has held power in the Republic since the revolution. While the plan does not bind the next government, it should be taken as a serious indication of basic government concerns and objectives for the new administration. The plan looks toward using the existing Foreign Investment Law more effectively to discourage the alleged use of legal devices designed to evade the spirit of Mexicanization. Among the devices referred to are the *fideicomiso*, pyramiding of holding companies that can give a foreigner effective control of what appear to be Mexican controlled companies, and the use of foreign loans or guarantees to pay the costs of an investment. The concern about the use of foreign loans and guarantees is that the foreign lender or guarantor may have more actual control than the Mexican shareholder's equity interest would indicate.

The *fideicomiso* is an object of increasing interest to both the government and the businessman. The PRI wonders whether the device is being used to evade the spirit of Mexicanization. The businessman wonders what will happen upon expiration of the life of the *fideicomiso*. The *fideicomiso* is a legal device similar to a common law trust whereby legal title is transferred to a third party, usually a Bank, for specific purposes and a limited time. The third party, called the *fideicomisario*, votes the shares. The beneficiaries of the *fideicomiso* receive the income from the shares. At the termination of the *fideicomiso*, the title to the shares is transferred from the *fideicomisario* to other parties under the terms of the *fideicomiso* or as the court directs. The Commission has yet to approve a *fideicomiso* with a life exceeding five years.

Few businessmen see such a short life as providing a means of evading ultimate transfer of the ownership of the shares to Mexicans. They do wonder how they will be able to sell those shares at more than distress prices if the current capital market structure is not revised to provide financial incentives for investment in equity issues. It is estimated that

company profits must reach 20% to 24% after taxes in order to provide the 12% to 14% yield now available to investors in the debt market. Businessmen feel that the burden is upon them to find the buyers and, failing that, their only alternative is a sale to a government agency. It may be that PRI's plan has foreseen such a situation. It speaks generally of a purchasing entity made up of state or mixed resources that would facilitate Mexicanization by acquiring stock in selected companies. The entity would be available to buy the stock when there are no private Mexican purchasers. Of course, there is the alternative of establishing an escrow, but it is difficult to see how an escrow is substantially different than a *fideicomiso*.

The experience of the past year under the Foreign Investment Law erases any doubt that it is increasingly being used as a tool to Mexicanize foreign controlled businesses that existed prior to the law's enactment. Notions that it is somehow being applied retroactively have gone aglimmering into the beguiling mists of the Mexican concept of *derechos adquiridos*. Businessmen accept its application as a fact of life and go forward. It would be a great comfort to businessmen if the government would accept as a fact of life the need for incentives to turn the investor away from fixed income debt instruments and toward equity issues. It could do this if it would go forward to enact a capital markets law that gave equity stock earnings a favored tax treatment and/or gave a favored tax treatment to gains on the value of the equity issues.

The past year has also seen the Commission move increasingly to the view that it is the duty of the investor to decide what matters shall be brought to the Commission. This duty is not clear from the law. Coupling this development with the increasingly broader scope the Commission gives to the meaning of concepts such as new establishment, new product line and new field of economics, there is a tendency on the part of some investors to elect not to report a doubtful move. They would rather face the prospect of the 100,000 peso fine than the prospect of opening the door to divestment in a close case.

This development brings into focus the question whether the Commission should issue guidelines. The Regulations of the National Registry published in the *Diario Oficial* on December 28, 1973 set up a procedure whereby the Commission may issue resolutions. These may be either "general" or "specific". General resolutions are public and may be published. Certain specific resolutions may be published as well. Thus there is authority and a legal structure within which guidelines may be issued.

The next question is then, is it a good idea for the Commission to publish guidelines or criteria? It has published four resolutions that expressed criteria and no discernible harm has come from them. Word has it that it has reached internal accord on several others, including one that sets forth criteria for defining a new establishment. Some say that the publication of criteria or guidelines will make the law too rigid, that once the standards have been expressed by government that the forces of politics are such that they cannot be changed. That view must be given great consideration. On balance, however, it seems that objective standards will make it easier for everyone to play the game. Guidelines can, therefore, encourage compliance with the spirit as well as the letter of the law by reducing the areas of uncertainty of application of the law. The investor will feel less threatened by the prospect of a fine and bad publicity, if there is less doubt about what actions he is expected to report to the Commission. Guidelines should be especially welcome if there is open consultation by the government with all affected sectors of the public before they are published. If the government encourages open consultations on such a matter, it is reasonable to believe that to the extent that businessmen are included in those consultations they will be encouraged to deal more openly with government.

In this connection, it is satisfying to report that the dialogue commenced last year between government officials of both the Executive Director's office of the Commission and the staff of the National Registry for Transfer of Technology has proceeded extremely well. Part Three of the paper will deal in more detail with this activity. It must be emphasized that it is the candid, informed exchange of views that has characterized this dialogue which should show the way toward purposeful consultation between the private sector and government. Such consultation can lead toward the formulation and publication of guidelines or criteria for the continued successful operation of the Foreign Investment Law.

The Technology Law

The thrust of the Registry's work continues to be concentrated on improving the negotiating posture of the Mexican licensee, identification and elimination of abusive licensing practices and furthering the development goals of the Republic. As set forth in Part One, the issues that occupied the Registry last year have continued to be more or less the same.

Two developments in the past year indicate major changes in the direction of the Registry. First, the Registry now views the transfer of

technology in the context of a purchase rather than as a license. It takes the position that in order to "renew" a contract the supplier must be able to show that the transferee is "acquiring" new technology. This change in direction has implications with respect to both the price paid for the technology and the duration of the contract. It would seem that if the technology acquired is being purchased, the price might well be higher. Since the transaction will be that of a sale, the duration of the contract would seem to take on the function of providing time within which the sale could be amortized.

This change in direction also raises the question of when a technology is ready for sale. There is almost always a ripening period from the time a technology has been developed until it has been proven in such a way as to justify its sale. The Registry's view that the transfer is a sale obviously serves Mexico's objective of actually acquiring technology. It also raises the question of the extent to which suppliers of technology may be less enthusiastic about entering into contracts with Mexican transferees for newly developed technology.

The second change in direction is the desire on the part of the staff of the Registry to begin to spend more of its time evaluating and auditing the contracts in effect. This is a singularly welcome development. We hope that the Registry staff will be able to look more closely at actual situations where technology is in the process of being transferred in Mexico. We are convinced that this exercise will prove enlightening because for some time licensors have contended that the transfer of technology may be as important as the development of it. In order for a technology to fit well into the productive capacity of the licensee there are many link-ups that must be made between the ideas and systems for production of a product or service and the capacity of the licensee to complete the idea and systems. Licensors have learned that this process is always long-term and usually requires the continuing presence of representatives of the licensor to insure that improvements on technology are properly integrated into the licensee's operations.

A third general development during the year has been the issuance by the Registry of general criteria with respect to Art. 7 of the law. These criteria or guidelines are designed to assist all parties who deal with the Registry to understand the general nature of clauses in contracts for technology transfer. The Registry is to be commended for the openness of this approach. The publication of these criteria should be another signal to businessmen of the Registry's continuing search for means of

establishing objective criteria in regulating technology transfer in Mexico. The criteria are very general and will undoubtedly be refined as the Registry adds to its experience in administering the law. It is the hope of the authors that the Registry will again request the comments and suggestions of the business community as refinements or changes are made in the criteria. It is regrettable that those organizations in the business community, which were asked for comment before the criteria were published did not respond. It should not surprise that this lack of response was a source of dismay to officials at the Registry. After all, there had been calls from the business community for the opportunity to make inputs before the criteria were published.

Specific issues of continuing interest include the price at which the technology is transferred, the companion issues of duration of the contract and confidentiality, and the status of trademarks. In the past year, the Registry also has placed new emphasis on the provisions of the law relating to the supplier's intervention in the administration of the transferee.

With respect to the fee or royalty that the user of technology may pay to the supplier, the Registry continues to refine its social cost/benefit approach. In the general criteria, recently published by the Registry, the statement is made:

In relation to this section (II of Art. 7), it is not possible to establish general rules that will permit the definition of what constitutes an adequate payment. That which is required, is a careful and detailed evaluation, from the technical-economic point of view, that would permit a definite determination of whether the payments to be made are in relation to the technical knowledge or the technology to be acquired, or if they constitute a justified charge for the national economy.

The Registry has, however, reached the firm conclusion that the cost/benefit considerations will be different for each economic sector. The ranges of rates approved on a case by case basis for contracts in various industries reflect the sectoral approach: pharmaceuticals, 6% to 10% of sales; light engineering and vehicles, 2.5% to 5% of sales; electronics, 4.5% to 5% of sales; food, 1% to 3% of sales and telecommunications, 5% of sales. These ranges of rates must be understood in proper context. They are neither minimums nor maximums. The Registry continues to approach the task of evaluating rates on a case by case basis.

The National Director of the Registry, Lic. Jaime Alvarez Soberanis, has recently acknowledged with approval the criteria set forth in the paper on Technology presented to this Committee last year. In an article that appeared in the July 1975 issue of *Jurídica* he said:

Hope H. Camp, and Clarence J. Mann, in an interesting study, have reached the conclusion that in the application of Section II of Art. 7, the Registry takes into account:

- a. the nature of the technology,
- b. the alternative sources of technology,
- c. the capital relationship between the contracting parties,
- d. the economic situation of the receiving company, and
- e. if there exist other unjustified charges in the contract.

The North American authors are correct in saying that these are some of the criteria that are often used by the Registry to evaluate the payments included in the contracts. We are able to say that, in summary, the administrative authority, carries out a cost/benefit analysis process in each actual case. The same study in the final part describes the general lines of this process which, while incomplete, is illustrative.

With respect to the *nature of the technology*, the Registry has looked very carefully at the age of the technology over the past year. Where a case for substantial increases in the productivity of the user could not be made, the Registry has moved to reduce payments requested. A negative age factor may be offset if the supplier can show that his technology has a dynamic impact on the economy. The supplier must show that despite its basic old age, it tends to generate economic activity that is consistent with national development goals. But where the technology, especially if it is sold, tends only to produce market growth for the user rather than greater profits, the Registry will likely press for lower payments to the supplier.

During the past year the Registry has continued to compare any particular technology with *alternative sources of technology* wherever they may exist in the world. The Registry continues to apply the criteria that was set forth in last year's paper:

1. What price is being charged by alternative sources of technology?
2. What similar technology is available domestically?

The Registry implements these two criteria through discussions with other governments and by shopping the domestic and international technology scene. In the course of this activity, the Registry is discovering, or perhaps is helping to create, a world-wide market for technology.

The third criteria mentioned by Lic. Alvarez in evaluating the price of technology is the *capital relationship between the supplier and the user*. The Registry continues its course in reducing royalty payments where there is a parent-subsidiary relationship. But even where there is no parent-subsidiary relationship, the Registry looks very carefully to see whether the user is dependent upon the supplier for materials, knowledge or economic support. One of the Registry's primary objectives is to convert a "weak user" into a "strong user" in the sense that the user will better be able to negotiate with the supplier. In this connection it continues to apply the "most favored licensee" principle which in general will prohibit a supplier from charging a price to the Mexican user that is any higher than that charged to a user in another country.

The economics of the licensee's operation continues to be the most important criteria governing price. The Registry has emphasized this past year that it will not approve fees which it believes to be disproportionate to either the sales, profits or net worth of the user. Although royalties based on a percentage of net sales continue to be approved, the Registry is still unconvinced that sales alone reflect the value of the technology to the user. Lacking more exact measuring devices, the Registry will approve percentage of sales royalties after comparing the cost with competing technologies and adding a strong social benefit flavoring.

Finally, the *unjustified burden* criteria has been used to prohibit exclusive grant-backs, production maximums, obligation of the user to pay Mexican or foreign taxes on royalties and the exclusive duty of the user to defend against patent infringements.

From our viewpoint the most troublesome issue currently facing the Registry with respect to price, is the search for formulas that will relate the price of a technology to its value to the society. Both businessmen and government officials have a lot of work to do with respect to surveying the impact of technology on society. Until the methodology of these surveys reaches a sufficient sophistication to *develop formulas* for evaluating technology, both the Registry and the businessmen who appear before it will continue to experience difficulty in establishing acceptable cost/benefit analyses of technology. A particular area which should be studied very

carefully by this Committee and its individual members is the special contribution of the private sector to economic development through combining entrepreneurial instincts and management expertise.

The next issue which deserves comment is actually a consideration of the companion issues of duration of the contract and the question of confidentiality. As you will recall the law limits contracts to a maximum term of ten years. This is a shorter term than the protection that is granted to industrial property, such as patents, under the existing Industrial Property Law. While many suppliers are concerned with the contracts being limited to a ten-year term, they are more concerned as to what could happen to industrial property secrets at the end of the term. It would appear that the use of non-disclosure contracts to suppliers would be one means of reducing this concern. Such contracts need not be registered. Suppliers are also concerned with protecting their secret processes in any improvements in the technology that might be passed along to the user during the term of the contract. With respect to this particular concern the Registry has adopted an automatic formula whereby the ten-year term does not start to run until the new technology has been disclosed.

In light of the Registry's position that the technology transfer shall be treated as a buy-sell transaction rather than a licensing transaction, the duration of the contract may become a function of the price. The price then will be based largely upon the value of the service that the supplier will transfer. Some suppliers have already been heard to say that they will not sell technology if it imperils their capacity to engage in competitive, profitable production at their home bases. They do not wish to give up industrial property secrets for the income from selling technology. They make more money producing the products than they do from selling the technology and industrial secrets that go with a technology sales contract.

Another interesting twist which is about to be added to the complex issue of confidentiality is the new Patent and Industrial Property Law which is in the process of being drafted. One provision of the projected law is alleged to require that patents be worked within three years or be lost. If this provision becomes law suppliers see a dilemma. The knowledge for making new products may not be safely transferred under a contract for technology sale unless production can be achieved within three years. Some suppliers say that such a provision of the law would discourage them either from registering patents or transferring any new developments to

Mexican licensees because quite often more than three years are required to prove the new patent to the point that it can be licensed.

The question of the future of trademarks continues to be discussed. The Registry continues to take a dim view of fees being paid for trademarks where there is an equity relationship between the owner of a trademark and the user. In the criteria recently published, the Registry has said that when there is no capital relationship between the licensor and the licensee, payments for the use of a mark shall be on the order of 1% of net sales. The same criteria goes on to say, however, that payments for royalties or marks will not be permitted if it is foreseen that the marks will be used for an indefinite term. This statement, of course, simply traces the philosophy of the law and the Registry in trying to encourage the development of Mexican trademarks.

A provision of the law which has received more attention this year than in the year past, is Section III of Art. 7 which prohibits intervention in the administration of the user's business by the supplier of technology. The criteria recently published by the Registry outlines the situation in which this clause will be the basis for denying a contract. First, the Registry will not approve the contract if it finds that the objective of the contract is the use of trademarks, patents or technical knowledge that will directly obligate the acquiring business to give up management totally or partially to the supplier of technology. The same will be true if the contract permits the supplier to obtain rights of disclosure in areas that go beyond the object of the contract. An example of such an object would be the granting to a supplier of a decision-making role in the marketing of the products manufactured by the user.

There is one other development in the past year with respect to technology which should be mentioned. This area concerns the proposed Codes of Conduct for the Transfer of Technology that are being debated internationally. A draft of such a code is the UNCTAD draft code written by the group of seventy-seven countries. The draft of the code is an attempt to set standards for the transfer of technology which will promote this transfer on equitable terms. From the point of view of any supplier the trouble with this proposed code is that it proceeds under the assumption that suppliers of technology normally take advantage of users of technology. Without granting or denying this assumption, it is fair to say that it is not based on very much objective fact about the actual value of technology. It is safe to say that very little is yet known about how to value technology. Under these circumstances we take the view that more

effort should be devoted searching for objective technology evaluation devices. If we know more about how to value technology we could more objectively determine whether suppliers are taking advantage of users. In addition, we ask the question whether it is sufficient to solve any of the real problems of transfer of technology by writing broadly worded codes in the absence of objective means for evaluating the worth of technology. We strongly urge that this Committee take the position that businessmen and world bodies, such as the United Nations, spend at least as much time developing methodology for evaluating the worth of technology as is spent in debating codes designed to regulate its transfer. We will have more to say as to how to go about valuing technology in the fourth part of this paper.

PART THREE

The third part of this paper is a report on the progress of the Task Force Program sponsored by this Committee. The first such meeting was held on September 23-24, 1974, and its results have been previously reported. At the request of the Mexican government people involved, the program for 1975 was modified as follows:

- * Meetings were to be sectorial, giving the opportunity to discuss a previously submitted list of issues between a group of representatives of different companies active in one industry segment, and the staffs of the Foreign Investment Commission and the Registry.
- * Meetings were scheduled in Mexico City with a duration of less than one day.

During 1975, the following meetings were scheduled:

1. Pharmaceuticals on January 13, 1975

The visiting group was formed by lawyers representing American Cyanamid, Schering, Merck Sharp & Dohme, Pfizer, and Johnson & Johnson. On the Mexican side, we had the Assistant to the Executive Secretary of the Foreign Investment Commission, the Director and two Sub-directors of the Registry and the Head of Patents of the Registry of Industrial Properties Department of the Secretariat of Industry.

2. Engineering Firms on April 10, 1975

The U.S. group included representatives from the Lummus Co., the Ralph M. Parsons Co., Foster Wheeler, Arthur G. McKee & Co., and

Arthur D. Little, Inc. Due to the nature of the issues, the Mexican group included the Director and Assistant Director of the Mexican equivalent of the I.R.S., in addition to the staffs of the Commission and the Registry.

3. Petrochemicals on October 23, 1975

Attending were representatives of Allied Chemical, Standard Oil Co. of Indiana, DuPont, and Exxon, from the U.S., and the staffs of the Commission and the Registry.

Before discussing some of the highlights of these meetings, their advantages and shortcomings, we believe that their atmosphere and flavor deserve a few lines. First of all, the U.S. groups were made up of people from the highest technical level, well versed in the problems of transferring technology and on the specifics of Mexican legislation in these matters. Second, the meetings were small, informal, frank, candid and honest, with each group showing understanding and appreciation for the other's problems, but still making its points and openly explaining its position on the issues. Discussions were heated at times, but always friendly and ending on a positive note.

As the more general issues have been covered in Part Two of this paper, we will refer here only to the specific problems raised by each industry segment, as we believe that these would not have been singled out otherwise.

Patents

As pointed out by the pharmaceutical industry group, Mexican patent legislation does not permit the patent of a product, extending protection only to the process used in its production. As a result, in order to assure adequate protection, companies need to patent not only the process that they intend to use, but also every other possible alternative. This situation results in a high number of patent applications for processes that are never going to be used.

Although it is clear that this situation results from the existing Mexican legislation on patents, it has produced a great deal of preoccupation in our government. The Secretariat of Industry has taken a hard look at the present status of patents in Mexico, and has concluded that the Patent Law in effect is not working on the basis of the following facts:

- * More than 90% of the patents are owned by foreigners.

- * Around 50% of the patents are granted to the pharmaceutical industry.
- * About 90% of the patents are never used.

As a result, a new law is being drafted and the project will be sent to Congress for enactment before December 31. It is reported that a draft will be available to the Mexican private sector by mid-November, with a request for comments in about one week. The new law appears to include some very controversial aspects, such as the reduction of the period of protection from fifteen to ten years.

Taxes

Engineering firms brought up two important problems associated with fiscal matters:

- * The I.R.S. does not permit tax credits for taxes paid in Mexico on work performed in the U.S. Tax credits are authorized only for taxes paid outside of the U.S. on work conducted also outside of the U.S. As a lot of the work done by these firms for Mexican clients is performed in the U.S., frequently they have to pay both U.S. and Mexican taxes.
- * The tax structure presently applied to services provided by engineering firms is equal to that applied to corporate profits, although the measure was aimed at the elimination of corporate tax evasion through payment of technical services not rendered, at a lower tax rate.

Both problems make engineering services more expensive to Mexico, and can even cause a withdrawal of these firms from the Mexican market. Government officials present indicated that a joint ad-hoc group has been formed between the I.R.S. and the Registry to study this problem.

Migratory Problems

Existing Mexican legislation in these matters makes the operation of engineering contracts very difficult, as it severely limits the required short term movement of foreign technicians in and out of Mexico.

Confidentiality

The issue of how to protect the supplier of technology from misuse of confidential information by the buyer after termination of the agree-

ment was raised by the petrochemical group, and produced a number of interesting answers:

- * The Registry feels that after termination of the agreement, the buyer *owns* the technology if he has made adequate payments for it.
- * In some cases, the Registry agrees with the principle of keeping confidentiality for ten years, starting from the time the buyer received the information.
- * Royalties should be lower when the supplier of technology has an equity position in the venture.

The fact that the Registry might consider that the buyer owns a technology after termination of the agreement, is an important change of attitude that can, in some cases, limit the flow of technology during the final years of a contract or even be unacceptable to some suppliers, who might elect not to transfer their technology under these conditions. We believe that additional meetings are required with the Registry to discuss this problem and clarify it further.

It is obvious the Task Force Program has already made significant contributions towards a better understanding of these two laws and their administration, for the benefit of all concerned. Those aspects of the program which represent its more positive effects and some suggestions on how to make it more interesting in the future will be discussed below.

Without question, the most significant contribution of this program has been the establishment of an open dialogue between foreign private businessmen and Mexican government officials at the technical level. The informal exchange of views has the following virtues:

- * Helps focus the issues and problems that face both sides.
- * Fosters private sector understanding of the pertinent laws.
- * Initiates contacts that can later be continued.
- * Helps modify the position of our government on certain issues through a better understanding of the other side's problems.

The program has won the support of those Mexican government officials concerned with these matters and, it is submitted, should be continued and expanded. The most important shortcoming of the program as it now stands, is the limited audience that its very nature imposes. The

more done to disseminate the results of these meetings, the better, as this will result in a better understanding of these two laws by greater numbers of potential foreign investors and, hopefully, in more investment. There are two ways to achieve this goal, i.e., by increasing the frequency of the missions to Mexico or by trying to organize tours in the U.S. for the heads of the Commission and the Registry.

Each of these alternatives has advantages and disadvantages and both need work from both sections of the Committee and a great deal of interest and support from Mr. de Maria and Mr. Alvarez. First, let us comment on the advantages and disadvantages of U.S. tours:

- * They represent an opportunity to reach greater numbers of people in their own, or in a nearby location.
- * Logistics become more difficult and their organization requires more preparation, time and money.
- * Their dedication and interest notwithstanding, both Mr. de Maria and Mr. Alvarez are extremely busy gentlemen. As a result, they cannot afford to be absent from their posts for too long or very often. The tours should be no longer than a week and probably not more than two per year.
- * While a meeting in Mexico facilitates the attendance of other top level members of the staffs of the Commission and the Registry and of representatives from other government offices as convenient, this is unlikely in the case of a U.S. tour.

The advantages and disadvantages of continuing the visits in Mexico are clearly the opposite in each case. As a logical next step, the next move should be to ask Mr. de Maria and Mr. Alvarez their opinions and suggestions, and/or pursue a course of action that will include the organization of at least one U.S. tour and two or three task force visits to Mexico in 1976.

PART FOUR

Two challenges are suggested by the first three parts of this paper. The first is how to develop governmental relations at the technical levels of government. The second is how to develop a methodology for evaluating the impact of management know-how coupled with the entrepreneurial instinct on economic development.

In the meetings and the discussions of this Committee for the past several years concern has been expressed for the future of the private sector. Among the developments over the past several years that have prompted this concern are restrictions on foreign investment and technology transfer throughout the world, attacks on the multi-national corporation, the proposal of codes of conduct designed to regulate the multi-national company and the transfer of technology. In Mexico we have been concerned about the lack of incentives for investment in the capital market, labor legislation that increases wages without reference to productivity, and government involvement in many areas previously the sole domain of private enterprise.

It may be more accurate to describe our reaction as businessmen as one of dismay rather than concern. We wonder why the politicians and even the public have not seen the benefits of private investment. We understand the importance of profits to economic development but others do not seem to. It appears that others have a greater belief in the government's ability to organize economic development projects than does the private sector. We are convinced, therefore, that we are misunderstood.

Businessmen and other representatives of the private sector have not stood idly by as this attack upon the private sector has mounted. Something is being done. Chambers of Commerce, other organizations and individual companies are engaged in programs of public relations designed to bring to the attention of the public and employees of private enterprise the benefits that this enterprise has upon the economy. The task force visits described in Part Three of this paper are another activity which helps to break down misconceptions about the private sector. Some individual companies have gone so far as to adopt codes of conduct in an effort to demonstrate that they are ready to voluntarily measure themselves against the signs of the times.

Nevertheless, it would appear that all of this effort is not enough to win the day. There seem to be gaps in the program of total education that must be undertaken to stem the attacks on the private sector and replace misconceptions with facts. While we do not propose the total answer to filling these gaps we would call your attention to the two challenges at the beginning of this part of the paper. We are convinced that there must be a more professional approach to governmental relations at the technical levels of government. Next we are convinced that in the process of dialogue with the technical levels of government, or for that

matter, in any kind of education program on behalf of the private sector, a package must be developed which will show the value of management know-how especially when it is coupled with entrepreneurial instincts.

Government Relations at the Technical Levels of Government

There are a few basic concepts that must be understood and accepted if we are to develop this approach to government relations.

First, the approach must be more professional and less personal. Second, a bridge of understanding and trust must be built on the basis of patient, time-consuming dialogue. Third, this approach can produce great benefits.

The traditional approach of businessmen in dealing with governments has been to develop personal relationships with top government officials. In the past, these kinds of relationships facilitated informal arrangements between government and private business that were useful. Nevertheless, the dialogue that developed from this kind of approach to government relations depended heavily upon personal relationships and commitments between top management and government officials.

In today's climate, the businessman must be prepared to supplement the more traditional personal approach of dealing with government officials at the high levels, with a more *professional, technically-oriented* approach for dealing with the technocrats who run the agencies. It is these technocrats who deal directly with the businessman on a myriad of matters including taxes, import permits, employee relations as well as investment and technology. The impressions and overall effectiveness of presentations made to these technocrats may well determine whether your problem is given the attention you believe it deserves.

Regardless of the level of professional excellence that is employed in making your presentation, you must have the confidence that you are being heard. That kind of confidence can only arise from mutual feelings of understanding and trust between the technocrat and the foreign investor. The businessman must try to build a bridge of understanding based on a new kind of *dialogue*. It is a two-sided exchange wherein you convince the technocrat that you understand his country's development goals before you try to sell him on the merits of your particular proposal. In the present atmosphere of misunderstanding of private investment, this may not be easy to do. But we must do it. We can do it by applying ourselves to studying and learning the country's development goals, the specifics

of its economic and political history, its current social problems and its laws. Having invested in the time and talent to develop this kind of understanding, we can develop presentations that will help to make our representatives credible as the dialogue progresses.

The dialogue that develops with the technocrats can be most *beneficial* in our program of replacing misconceptions with understanding and trust. It can lead to the development of objective standards for applying these laws. The technocrat will transmit his views to you on how the law is meant to work. You, the private businessman, will transmit your views on why a particular application of the law is harmful to your operation. Out of such an exchange, mutual accommodation may develop. At the very least there will be greater mutual understanding. This kind of dialogue can help to create a climate of openness that can lead to the establishment of objective standards for the application of laws. As objective standards begin to be developed, it will be easier for the representative of private business to discuss his plans for the future with government officials. The government will be inclined to be more open with respect to its decision-making processes. A more objective and open government decision-making process should enable the businessman to make more informed investment decisions.

Thus, we are presented with the challenge of how to develop the specifics of the proposed dialogue between the businessman and the technical levels of government. The elements of developing such a dialogue appear to me to include the following:

1. A definition of objectives.
2. An understanding of the elements of effective communication with the technical levels of governments.
3. An understanding of the need for a professional governmental relations counselor.
4. The proper selection of a governmental relations counselor.

The businessman must decide at the outset exactly what his objectives are in undertaking a governmental relations program at the technical levels of government. Those objectives should include as a minimum the following:

1. Constructive input to the government official.
2. A recognition and acceptance of the political realities of the given situation.

3. Communication of a sincere belief in the concept of open communications with the government.

Constructive input to the technocrats should be pitched toward helping the technocrat do his job well. A very constructive beginning point is to tell the story of your own company. It is something that you know well and it is a story that the government official wants to know. Regardless of how long you may have operated in a given country or in how many different ways that story has been told you will find government officials, especially at the technical levels, that do not know it. Tell your story in terms of the dynamic impact your company's operations have had in developing job opportunities, creating or expanding opportunities for local suppliers and bringing new technology or "know-how" to their economies. Tell the story in terms of your company's strict observance of national laws and support of worthwhile charitable and civic activities. The telling of your own story cannot but help to point up the positive impact of private investment in helping the country meet its development priorities.

If your company has done economic studies alone or in cooperation with other companies, bring them to the technocrat's attention. Discuss the weak points and the strong points of the study. If the study relates to the amount of foreign investment in the country and it shows substantial increases in recent years, point out the benefits of such investment but be ready to acknowledge potential problems. If your company has not participated in such a study ask yourself: why not? Such a study provides a basis for helping the technocrat do his job better because it should present an objective and balanced view of whatever is studied. In addition to telling your own company's story, or the story of a study, be able to talk in general about what is happening in the technocrat's own country. Be ready to demonstrate an understanding of some of the problems that his government faces in attaining its social and economic goals. Like the rest of us, the technocrat is overworked and does not have all of the time he needs to read and reflect. He will appreciate the opportunity to share his insights with those of the businessman in a non-adversary context.

The businessman must recognize that the dialogue with the technocrat is not the place for political *debate*. He must recognize and accept the political realities of the country in which he is doing business or in which he wishes to do business. Nothing is to be gained and a great deal is to be lost by wasting the technocrat's time in discussions of the political or economic philosophies that form the basis of laws such as the one we

are considering. The laws are on the books and must be accepted. The value of the dialogue with the technocrat should be to look for ways in which the private investor can maximize his business opportunities within the existing framework of law.

The private investor must communicate a sincere belief in the concept of open communication with his counterparts in the government. A good first step is to listen; act as a sounding board. Developing this aspect of the approach to government officials at the technical level is both more important and more difficult than might at first appear. It is important because it builds person to person trust that, with solid facts, can be translated into belief in the value of the private investor's role in the country. It is difficult because one must resist the temptation to always talk about the problems that concern his own investment.

Regular contact with the technocrats in the agencies helps to reinforce your desire for open communication. Although each situation will vary, try to see your contacts at least once every two weeks, unless this is inconvenient for the government official. The meetings need not be long. You must be sensitive to the time demands of the technocrat. They need not always include a long luncheon or an elaborate dinner. Periodic breakfasts seem to be coming more into vogue. Of course, all meetings should be cordial but businesslike. Before any meeting prepare yourself to be able to impart news or insights of specific use to the government official.

The second element of effective government relations is to identify the basic activities that must be undertaken to establish effective dialogue with the technical levels of government. The first activity is a collection of information with respect to governmental actions. Next, that information must be analyzed within the framework of the local economic, social and political considerations. Next, there must be developed from the analysis of this information, constructive responses to government actions that affect the private investor. Finally, there must be developed effective vehicles and methods for communicating these responses to the government.

The activity of collecting information with respect to governmental agencies entails reading everything that is available with respect to the activities of the governmental agencies affecting your business. It entails maintaining regular contact with the agencies. This is one of the most effective ways of sensing in advance new trends in government thinking

that portend government action that may affect your business. Another good source of knowledge is for your representative to play an active role in the legislative or other government related committees of trade or business associations.

As this information is being gathered, it must be organized and analyzed to establish a basis upon which management can evaluate the significance of actual, probable or possible government action that may affect your business. The process of analysis should include discussion and debate among your management teams. The analysis should include internal memoranda outlining the facts, the issues raised by the facts and a scenario of the consequences including financial impact data when not irrelevant. From the information analyzed it will be possible to develop a strategic approach to government relations. Few issues arise in a vacuum. Every effort should be made to see the particular problem under consideration in relation to other problems, and within the general economic and political framework of the country. Of course, the exercise must not be academic. Focus on your immediate problem and develop a response.

Having developed an appropriate response to a particular government action, you should endeavor to coordinate the content and timing of your response with other private investors and/or business organizations in the country. Sometimes such coordination will not be possible due to lack of time or even lack of a community of interest on a given issue. When you are able to coordinate your response, however, you will obtain valuable insights that may enable you to improve it.

When you have completed the coordination exercise then you must decide how the response will be presented to the government. There are many forms and structures for communicating your response. Naturally, you can do it through informal conversations as a part of the continuing dialogue that you have already established with the technocrat. At times, it may be useful to present a memorandum without comment. At other times, it may be necessary to present the memorandum in connection with a visit to the government official. At other times, it may be necessary to use the media for communicating the response. The response may be communicated by the private investor alone or under the sponsorship of a trade association. The response may be communicated by a group of private investors having similar interests. One thing is clear: with respect to the vehicle of communications, it will probably not be the same for every situation, and it will probably be a combination of contacts and different methods of written, oral and person to person communication.

The third element of effective governmental relations at the technical level is for each investor to select a professional governmental relations counselor. Management executives normally do not have the time to devote to establishing the desired dialogue. It is truly a daily activity and a full-time job. Perhaps the only question the foreign investor must ask is whether the expense of such a specialist is justified. For most large private investors the expense of such a professional is negligible in relationship to the benefits of an effective representation. Management executives are normally generalists or have come up through the ranks for the company that they work for. They have excellent knowledge of the company and the business but do not have a special knowledge of the laws and economics of the country. And let me say again, usually they do not have the time to develop sufficient special knowledge in these areas to feel confident in dialogue with the technocrat. Thus, a selection of the proper person to serve as the governmental relations counselor is the key to an effective governmental relations program. An improper selection will do more harm than not having such a counselor at all. The criteria for the selection of such a person should include the following: The counselor should be a professional with a background in economics, business, law or political science. These types of backgrounds help to insure disciplined conduct in dealing with government officials as well as a sound intellectual approach to the job. The counselor should be a native of the country or strongly rooted in its culture and should be completely fluent in the language of the country.

The government relations counselor should be capable of playing an active role in the business organizations of which your company is a member and those that it supports. The counselor should function mainly as a catalyst for helping those organizations help their members in developing positions that can be communicated to the government. He should, as much as possible, remain in the background to preserve his integrity with his governmental contacts. If he becomes too visible as a spokesman for the private investor, he will begin to lose his ability to communicate openly and to receive open communications from government officials. The counselor should work quietly and patiently to build bridges of understanding between the private businessman and the government. He has a special role as a teacher with respect to his own management. He must acquaint the management with the language of the technocrat and with concepts such as the cost/benefit analyses referred to previously. He must teach his management how to use that language and those concepts as a framework for explaining how their businesses are contributing to the development goals of the country.

An on-going professional approach to governmental relations at the technical levels of government equips the businessman to respond quickly, positively and constructively when the government begins to formulate plans of action. Such a program assumes a legitimate partnership in the process of governing with government, labor and other identifiable sectors of the community. It assumes that the ideas and informed thinking of the businessman are welcomed by the government. Finally, it assumes that when government asks the business community for its views, as the Registry of Technology did before it published its criteria, that the businessmen will respond.

Need to Develop Methodology for Evaluating Management Know-How

It is well to have governmental relations and public relations programs that tell the story of how private enterprise contributes to the development goals of the country. We suggest, however, that something more needs to be said than generally outlining contributions toward increased employment opportunities, construction of plant sites in less developed areas of the country and contributions to export sales. These kinds of contributions could be made by government companies supported by tax dollars. What the private sector needs to add to the story that it is telling is a way of explaining the unique contribution of management know-how coupled with the entrepreneurial instinct. It needs a way of explaining that private enterprise management is a key factor in producing the tax dollars that are necessary for any government program. Even more specifically, the private sector needs objective devices for demonstrating how private sector management adds a special dimension to the efficiency of plant operations, the development of new products, effective training programs and employee benefit programs.

The beginnings of the search for these objective standards may have already begun as governments and companies try to develop accurate cost/benefit analyses of technology. Technology audits are being undertaken by companies, in particular, to explain to governments the value of their technology. In the course of these audits it has been discovered that a key factor, if not the key factor, in transmitting the technology is the on-site management representatives of the supplier of the technology. The basic question raised by these audits is what would happen if the on-site management team were removed from the scene. Is the operation sufficiently self-generating to continue without this input or is there a need for continuing input from these managers in order to sustain the

dynamic development of the technology? From a slightly different viewpoint we ask, is the multiplier effect of an investment or a technology transfer capable of being continued without management oriented to risk taking for profit? By multiplier effect, we mean the dynamic impact of an investment on a technology transfer upon related businesses, employment and general economic activity.

The answer to these questions may lie in developing methods of surveying the impact of management know-how. The surveys might include statistical measurements of production or service, comparisons of performance with competition including government operations, employment opportunities, training, and the extent to which research and development will continue without the on-site management team. From such surveys might come formulae for expressing the value of management in terms of the cost/benefit analysis currently relied upon by the technical levels of government in evaluating investment or technology proposals. Not only would these formulae serve the governmental relations purpose of explaining the merits of a proposed investment or a technology transfer, but they would also serve the broader purpose of explaining why the private sector has a special contribution to make to economic development. In addition, such formulae would aid businessmen in negotiations with prospective partners and could even serve the internal purpose of valuing the services of the managers themselves.

We look for a way of finding a methodology for measuring the value of management know-how. We proceed on the theory that such a methodology would serve the practical purposes we have mentioned. At the very least, this theory deserves the same degree of attention and discussion as the codes of conduct are receiving. We believe that such an exercise will show the way toward making an even more objective case for the private sector that can effectively challenge misconceptions that now abound. We do not take the view, especially with respect to Mexico, that the current antagonistic attitudes towards the private sector are so politicized that the bright light of hard fact cannot cut the fog of misconceptions. We, therefore, urge this Committee and its individual members to consider ways and means of supporting the concept of a survey of management know-how for the purpose of developing formulae that will enable the private sector to objectively demonstrate its worth, whenever and wherever such a demonstration is required.